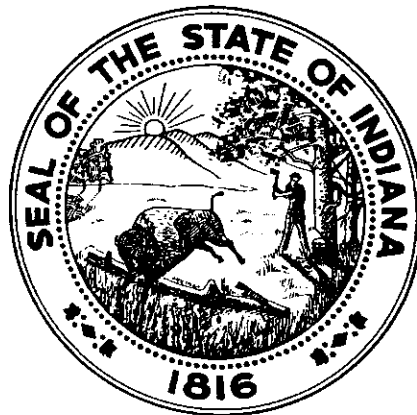


STATE BOARD OF ACCOUNTS
302 West Washington Street
Room E418
INDIANAPOLIS, INDIANA 46204-2765

AUDIT REPORT
OF
INDIANA STATE TEACHERS' RETIREMENT FUND
STATE OF INDIANA
July 1, 2001 to June 30, 2002



Signature Valid

Indiana State Board of Accounts

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State Board of Accounts
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AGENCY OFFICIALS

<u>Office</u>	<u>Official</u>	<u>Term</u>
Director	Dr. William E. Christopher	04-15-99 to 01-10-05
President of the Board	Mr. Matthew B. Murphy, III	01-07-00 to 11-30-03



STATE OF INDIANA
AN EQUAL OPPORTUNITY EMPLOYER

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INDEPENDENT AUDITORS' REPORT

TO: THE OFFICIALS OF THE INDIANA STATE TEACHERS' RETIREMENT FUND BOARD OF TRUSTEES

We have audited the accompanying basic financial statements of the Indiana State Teachers' Retirement Fund, as of and for the year ended June 30, 2002. These basic financial statements are the responsibility of the Indiana State Teachers' Retirement Fund Board of Trustees' management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the basic financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Note 1 to the financial statements, the Indiana State Teachers' Retirement Fund Board of Trustees has adopted Governmental Accounting Standards Board Statement No. 34, Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments, as amended, for the year ended June 30, 2002.

In our opinion, the basic financial statements referred to above present fairly, in all material respects, the plan net assets of the fiduciary funds of the Indiana State Teachers' Retirement Fund Board of Trustees as of June 30, 2002, and the changes in the plan net assets of the fiduciary funds for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis, Schedule of Funding Progress, Schedule of Employer Contributions, and the Notes to Required Supplemental Schedules are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board.

We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of required supplementary information. However, we did not audit the information and express no opinion on it.

STATE BOARD OF ACCOUNTS

October 31, 2002

INDIANA STATE TEACHERS' RETIREMENT FUND MANAGEMENT'S DISCUSSION AND ANALYSIS

This section presents management's discussion and analysis of the Indiana State Teachers' Retirement Fund (TRF) financial statements for the year ended June 30, 2002. The MD&A is presented as a narrative overview and analysis. The MD&A should also be read in conjunction with the financial statements, the notes to the financial statements, and the supplementary information.

FINANCIAL HIGHLIGHTS

- The net assets of TRF were \$5.7 billion as of June 30, 2002.
- The net assets of TRF decreased by \$88 million, or 1.5% from the prior year. The decrease was primarily due to adverse equity markets, resulting in lower investment values.
- The TRF rate of return on investments for the year was negative 2.4% on a market value basis, compared to last year's positive 2.1%, due primarily to the continued downturn in world equity markets.
- As of June 30, 2001, the date of the most recent actuarial valuation, the Pre-96 plan (Closed Plan) is actuarially funded at 42.2%, which is more than the 42.0% funded level as of June 30, 2000. The 96 plan (New Plan) is actuarially funded at 54.0%, which is more than the 52.2% funded level as of June 30, 2000. The closed plan includes all members who were hired before July 1, 1995, and have been continuously employed by the same board of education as they were on that date. The new plan includes all other members.

OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to TRF's financial statements. The financial section of the TRF Annual Financial Report is comprised of three components: (1) TRF's financial statements, (2) notes to the financial statements, (3) required supplementary information. The information available in each of these sections is briefly summarized as follows:

(1) Financial Statements

The statement of plan assets presents information on TRF's assets and liabilities and the resulting net assets held in trust for pension benefits. This statement reflects TRF's investments, at fair value, along with cash and short-term investments, receivables and other assets and liabilities. This statement indicates the net assets available to pay future pension benefits and gives a snapshot at a particular point in time.

The statement of changes in plan net assets presents information showing how TRF's net assets held in trust for pension benefits changed during the years ended June 30, 2002 and 2001. It reflects contributions by members and employers along with deductions for retirement benefits, refunds, and administrative expenses. Investment income and losses during the period are also presented showing income from investing and securities lending activities.

(2) Notes to the Financial Statements

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in TRF's financial statements.

(3) Required Supplementary Information

The required supplementary information consists of a Schedule of Funding Progress and a Schedule of Employer Contributions and related notes concerning the funding status of TRF.

INDIANA STATE TEACHERS' RETIREMENT FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

FINANCIAL ANALYSIS

Total assets of TRF were \$6.8 billion as of June 30, 2002, compared with \$6.6 billion as of June 30, 2001. The increase in total assets was primarily due to investments purchased at year end that had not settled and been paid for until the beginning of the next fiscal year.

Total liabilities were \$1.1 billion as of June 30, 2002, compared with \$.8 billion as of June 30, 2001. The increase in total liabilities was due to a increase in investments purchased at year end that did not settle until the next fiscal year.

A summary of TRF's Net Assets is presented below:

NET ASSETS (\$ in thousands)			
	June 30, 2002	June 30, 2001	% Change
Assets:			
Cash and Cash Equivalents	\$ 743,438	\$ 331,333	124.4%
Securities Lending Collateral	553,452	586,199	(5.6%)
Receivables	272,155	201,417	35.1%
Investments	5,265,798	5,502,486	(4.3%)
Other Assets	46	13	253.8%
Total Assets	6,834,889	6,621,448	3.2%
Liabilities:			
Securities Lending Collateral	553,452	586,199	(5.6%)
Other Current Liabilities	558,587	224,309	149.0%
Long-Term Liabilities	98	180	(45.6%)
Total Liabilities	1,112,137	810,688	37.2%
Total Net Assets	\$ 5,722,752	\$ 5,810,760	(1.5%)

As the above table shows, plan net assets were \$5.7 billion as of June 30, 2002, a decrease of \$88 million, or 1.5%, compared to the prior year, driven by the decrease in market value of investments during the year.

The following table presents TRF's investment allocation compared to TRF's target investment allocation and the prior year allocation.

	June 30, 2002 Actual	June 30, 2002 Target	June 30, 2001 Actual
Fixed Income	46.3%	40.0%	57.4%
Large Cap Equity	26.6%	24.5%	22.9%
Mid Cap Equity	5.9%	5.25%	5.3%
Small Cap Equity	4.4%	5.25%	6.4%
International Equity	16.7%	15.0%	8.0%
Private Equity	0.1%	5.0%	0.0%
Real Estate	0.0%	5.0%	0.0%
Total	100%	100%	100%

INDIANA STATE TEACHERS' RETIREMENT FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

The change in weightings between asset classes was driven by new target allocations, which were adopted by TRF during the year ended June 30, 2002. As a result, investment manager searches were initiated. Upon completion of the manager searches and contract negotiations, new allocations for Private Equity and Real Estate will be funded, bringing the investments closer to the targeted allocations. At June 30, 2002, the 5% target for Real Estate was invested in Fixed Income and will be drawn from there as suitable real estate investments are made. The remaining Private Equity target allocation of 4.9% will be drawn from the Large Cap Equity investments.

A summary of the changes in net assets during the years ended June 30, 2002 and 2001 is presented below:

CHANGES IN NET ASSETS (\$ in thousands)

	FY Ended June 30, 2002	FY Ended June 30, 2001	% Change
Additions:			
Member Contributions	\$ 107,052	\$ 104,523	2.4%
Employer Contributions	541,083	537,892	0.6%
Contributions to Pension Stabilization Fund:			
From State Lottery	30,000	30,000	0.0%
From the State of Indiana	-	125,000	N/A
Net Investment (Loss) Income	(158,320)	25,733	(715.2%)
Transfers From Public Employees' Fund	1,254	2,379	(47.3%)
Other	2,153	5,433	(60.4%)
Total Additions	<u>523,222</u>	<u>830,960</u>	37.0%
Deductions:			
Benefits	594,718	580,170	2.5%
Refunds	6,450	8,754	(26.3%)
Transfers to Public Employees' Fund	1,251	2,057	(39.2%)
Capital Projects	1,239	2,029	(38.9%)
Administrative Expenses	6,793	4,775	42.3%
Claims on Outdated Benefit Checks	778	-	N/A
Total Deductions	<u>611,229</u>	<u>597,785</u>	2.2%
Increase (Decrease) in Net Assets	<u>\$ (88,007)</u>	<u>\$ 233,175</u>	(137.7%)

ADDITIONS

Additions needed to fund benefits are accumulated through contributions from members and employers and returns on invested funds. Member contributions for the year ended June 30, 2002, totaled \$107.0 million. This represents an increase of \$2.5 million or 2.4% compared to the prior year. Employer contributions were \$541.1 million, an increase of \$3.2 million or 0.6%.

The State of Indiana made a special contribution to the Pension Stabilization Fund in the prior fiscal year of \$125.0 million. This contribution was not made during the fiscal year ending June 30, 2002.

INDIANA STATE TEACHERS' RETIREMENT FUND
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

TRF recognized a net investment loss of \$158.3 million for the year ended June 30, 2002, compared to a net investment gain of \$25.7 million in the prior year. The higher investment losses were primarily due to the continued adverse equity markets, which resulted in a loss of 17.4% on TRF's domestic large cap equity investments. This compares to a loss of 18.0% for the S&P 500 index during the year. Domestic Mid Cap equities had a loss of 8.45% as compared to a loss of 4.73% for the S&P 400 Mid Cap index during the fiscal year. Domestic Small Cap equities had a loss of 3.99%, as compared to a loss of 8.57% for the Russell 2000 index during the fiscal year. International equities had a loss of 11.77%, as compared to a loss of 9.23% for the EAFE index during the fiscal year. Investment losses on equities were partially offset by TRF's fixed income portfolio, which achieved a total return of 5.29% for the year ended June 30, 2002. The total rate of return on TRF's investments was a negative 2.38% compared to a positive 2.1% in the prior year.

DEDUCTIONS

The deductions from TRF's net assets held in trust for pension benefits include primarily retirement, disability, and survivor benefits, refunds of contributions to former members, and administrative expenses. For the year ended June 30, 2002, benefits amounted to \$594.7 million, an increase of \$14.5 million or 2.5% from the prior year. The increase in benefits was due to an increase both in the number of retirees and the average benefit paid. Refunds to former members were \$6.4 million, which represents a decrease of 26.3% over the prior year.

Administrative expenses were \$6.8 million, an increase of \$2.0 million compared to the prior year. The fiscal year ending June 30, 2002, amount includes a one-time cost of \$2.6 million for data processing system development. The fiscal year ending June 30, 2001, included a one-time cost of \$1 million for Y2K programming charges.

HISTORICAL TRENDS

A pension fund is well funded when it has enough money in reserve to meet all expected future obligations to participants. The funded ratios of the defined benefit pension plans administered by TRF as of the latest actual valuations were as follows:

	<u>July 1, 2001</u>	<u>July 1, 2000</u>
Pre-96 Plan (Closed Plan)	42.2%	42.0%
96 Plan (New Plan)	54.0%	52.2%

An analysis of the funding progress, employer contributions, and a discussion of actuarial assumptions and methods is set forth in the required supplementary information section of the financial statements.

INDIANA STATE TEACHERS' RETIREMENT FUND
STATEMENT OF FIDUCIARY NET ASSETS
June 30, 2002

Assets

Cash and Cash Equivalents	\$ 743,438,282
Securities Lending Collateral	<u>553,452,342</u>
Receivables:	
Employer Contributions	27,981,632
Due From PERF	4,217,073
Member Contributions	28,270,489
Due From Lottery Commission	7,500,000
Securities Sold	166,877,930
Investments Interest	<u>37,308,246</u>
Total Receivables	<u>272,155,370</u>
Investments:	
U.S. Treasury and Agency Obligations	1,555,781,310
Corporate Bonds and Notes	1,446,005,967
Foreign Bonds	12,718,800
Equity Securities	2,251,031,816
Real Estate	<u>260,000</u>
Total Investments	<u>5,265,797,893</u>
Furniture and Equipment (Original Cost of \$411,959 Net of \$365,873 Accumulated Depreciation)	<u>46,086</u>
Insurance Premium Paid in Advance	<u>27</u>
Total Assets	<u>6,834,890,000</u>

Liabilities

Accrued Benefits Payable	3,243,947
Accrued Salaries Payable (See Note 1)	131,433
Accrued Liability for Compensated Absences - Current	119,816
Accounts Payable	4,137,451
Due To PERF	6,460,896
Securities Lending Collateral	553,452,342
Payables for Securities Purchased	<u>544,492,904</u>
Total Current Liabilities	<u>1,112,038,789</u>
Accrued Liability for Compensated Absences - Long-Term	<u>98,031</u>
Total Liabilities	<u>1,112,136,820</u>
Net Assets Held in Trust for Pension Benefits (See Schedule of Funding Progress, Page 18)	<u>\$ 5,722,753,180</u>

The accompanying notes are an integral part of the financial statements.

INDIANA STATE TEACHERS' RETIREMENT FUND
STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS
Year Ended June 30, 2002

Additions:

Contributions

Member Contributions	\$ 107,051,946
Employer Contributions	541,082,604
Employer Contributions - Pension Stabilization	<u>30,000,000</u>

Total Contributions	<u>678,134,550</u>
---------------------	--------------------

Investments

Net Appreciation (Depreciation) in Fair Value	(383,396,789)
Interest Income	215,666,179
Dividend Income	19,924,600
Securities Lending Income	13,817,498
Less Investment Expense	
Investment Fees	(12,090,707)
Securities Lending Fees	<u>(12,240,479)</u>

Net Investment Income	<u>(158,319,698)</u>
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Other Additions

Transfers From Other Retirement Funds	1,253,717
Annuity and Disability Refunds	1,287,032
Outdated Benefit Checks	864,581
Reimbursement of Administrative Expense	<u>1,931</u>

Total Other Additions	<u>3,407,261</u>
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Total Additions	<u>523,222,113</u>
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Deductions:

Annuity and Disability Benefits	594,717,533
Voluntary and Death Withdrawals	6,449,874
Claims on Outdated Benefit Checks	777,953
Administrative Expenses	6,780,919
Capital Projects	1,238,838
Depreciation Expenses	12,745
Transfers to Other Retirement Funds	<u>1,250,635</u>

Total Deductions	<u>611,228,497</u>
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Change in Net Assets Held in Trust for Pension Benefits	(88,006,384)
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Net Assets Beginning of Year	<u>5,810,759,564</u>
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Net Assets End of Year	<u>\$ 5,722,753,180</u>
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The accompanying notes are an integral part of the financial statements.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002

Note 1. Summary of Significant Accounting Policies

- A. Reporting Entity - The financial statements presented in this report represent only those funds that the Indiana State Teachers' Retirement Fund (TRF) has responsibility for and are not intended to present the financial position or results of operations of the State of Indiana or all of the retirement and benefit plans administered by the State. Effective July 1, 2001, TRF became an independent corporate and politic (Public Law 119-2000). TRF is not a department or agency of the State but is an independent body corporate and politic exercising essential government functions. The members of the Board of Trustees of the Indiana State Teachers' Retirement Fund are appointed by the Governor of the State of Indiana and a financial benefit/burden relationship exists between the TRF and the State of Indiana. For these reasons, TRF is considered a component unit of the State of Indiana for financial statement reporting purposes.
- B. Basis of Presentation - The financial statements of the Indiana State Teachers' Retirement Fund have been prepared using fund accounting in conformity with generally accepted accounting principles (GAAP) as applied to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standards setting body for established governmental accounting and financial reporting principles. GASB Statement 25 has been implemented for the defined benefit pension plans.

In June of 1999, the GASB issued Statement No. 34 (the "Statement") Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments. This Statement establishes financial reporting standards for state and local governments. The requirements of this Statement are effective for periods beginning after June 15, 2001, in three phases based on a government's total annual revenues in the first fiscal year ending after June 15, 1999. This Statement has no impact on TRF's net assets, but does require certain changes to the presentation of the financial statements and additional disclosures. With these financial statements, PERF is implementing these changes and accordingly, has included Management's Discussion and Analysis as required by the Statement.

- C. Fund Accounting - Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain governmental functions or activities. The Indiana State Teachers' Retirement Fund is a pension trust fund. For a description of this fund, see Note 2.
- D. Basis of Accounting - The records of this Fund are maintained on a cash basis. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows.
- E. Budgets - A budget for the administrative expenses is prepared and approved by the Board of Trustees.
- F. Deposits and Investments - The Treasurer of State acts as the official custodian of the cash and securities, except for securities held by banks or trust companies under custodial agreements with the Board of Trustees. The Board of Trustees may contract with investment counsel, trust companies, or banks to assist the Board in its investment program. The Board is required to diversify investments in accordance with prudent investment standards. The Board has issued investment guidelines for its investment program which authorized investments of: U.S. Treasury and Agency obligations, U.S. Government securities, common stock, international equity, corporate bonds, notes and debentures, repurchase agreements secured by U.S. Treasury obligations, mortgage securities, commercial paper, and banker's acceptances. See Note 4 for more details.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002
(Continued)

- G. Method Used to Value Investments - Investments of defined benefit plans are reported at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. Investments that do not have an established market are reported at estimated fair value.
- H. Equipment - Equipment with a cost of \$5,000 or more is capitalized at the original cost. Depreciation is computed on the straight-line method over the estimated five year life of all assets.
- I. Contributions Receivable - The contributions receivable was determined by using actual contributions received in July for days paid in the quarter ended June 30, 2002.
- J. Inventories - Inventories of consumable supplies are not recognized on the balance sheet as they are considered immaterial. Purchases of consumable supplies are recognized as expenditures at the time of purchase.
- K. Reserves and Designations

The following are the legally required reserves and other designations of fund equity:

1. Member Reserve: This member's reserve represents member contributions made by or on the behalf of the employees plus any interest distributions, less amounts refunded or transferred to the Benefits in Force reserve for retirement disability, or other benefit. For Indiana State Teachers' Retirement Fund this reserve is the employees' annuity savings account.
2. Benefits in Force: This reserve represents the actuarially present value of future benefits for all members who are presently retired or disabled. The accumulated contributions of the members are transferred to the reserve upon retirement or disability. The remainder of the actuarial pension cost is transferred from the employer reserve to fund the benefits. This reserve contains \$1,786,817,879 for the Pension Stabilization Fund. The Pension Stabilization Fund was established by IC 21-6.1-2-8.
3. Employer Reserves: This reserve consists of the accumulated employer contributions plus earnings distributions less transfers made to the Benefits in Force reserve of the actuarial pension cost.
4. Undistributed Investment Income Reserve: This reserve was credited with all investment earnings. Interest transfers have been made annually to the other reserves as allowed or required by statutes. The transfers are at rates established by the Board of Trustees.
5. Unreserved Fund Balance: This reserve represents the unfunded actuarial accrued liability for non-retired participants, determined by the fund's actuary, as of the date of the last valuation.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002
(Continued)

The following are the balances of the reserves and designations of fund equity:

<u>Member Reserve</u>	<u>Employer Reserve</u>	<u>Benefits In Force</u>	<u>Undistributed Income</u>	<u>Unreserved Fund Balance</u>
<u>\$ 2,637,014,113</u>	<u>\$289,162,091</u>	<u>\$ 2,618,345,964</u>	<u>\$180,572,866</u>	<u>\$ (7,713,066,409)</u>

- L. Payables and Liabilities - Payables and liabilities are not maintained throughout the year on the accounting records. They are calculated or estimated for financial statement reporting purposes and are posted to the general ledger at year end.
- M. Compensated Absences - TRF's full-time employees are permitted to accumulate earned but unused vacation and sick pay benefits. Vacation leave accumulates at the rate of one day per month and sick leave at the rate of one day every two months plus an extra day every four months. Bonus vacation days are awarded upon completion of five, ten and twenty years of employment with the State of Indiana. Personal leave days are earned at the rate of one day every four months; any personal leave accumulated in excess of three days automatically becomes part of the sick leave balance. Upon separation from service, employees in good standing will be paid for a maximum of thirty unused vacation leave days.

No liability is reported for unpaid accumulated sick leave. Vacation and personal leave and the salary-related payments that are expected to be liquidated are reported as Compensated Absences Liability.

Note 2. Fund Description

The Indiana State Teachers' Retirement Fund is the administrator of a multiple-employer retirement fund established to provide pension benefits for persons who are engaged in teaching or in the supervision of teaching in the public schools of the state or persons who are employed by the fund. At June 30, 2002, the number of participating school unit employers was:

Public School Units	317
Higher Education Units	4
State of Indiana Agencies	33
Associations	<u>3</u>
Total	<u>357</u>

Membership in the Fund is required for all legally qualified and regularly employed teachers who serve in the public schools of Indiana, including the faculty at Vincennes University, and employees of Fund. Additionally, faculty members at Ball State University, Indiana State University, and University of Southern Indiana have the option of selecting membership in the Fund or the alternate University Plan. As of July 1, 2001, Indiana State Teachers' Retirement Fund membership consisted of:

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002
(Continued)

Retirees and Beneficiaries Currently Receiving Benefits	33,783
Active Plan Members	75,648
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	<u>4,595</u>
Total	<u>114,026</u>

The Indiana State Teachers' Retirement Fund provides retirement benefits, as well as death and disability benefits. Eligibility to retire occurs at age fifty with fifteen or more years of service or at age sixty-five with ten years of service. Annual retirement benefits, disability benefits, and death benefits are computed as follows:

Regular Retirement (No Reduction Factor For Age)

Eligibility - Age sixty-five with ten years service or age sixty with at least fifteen years of service or age fifty-five with age plus years of service equaling at least eighty-five.

Mandatory Retirement Age - none.

Annual Amount - State pension equal to total years of service times 1.1% of final average salary; plus an annuity purchased by the member's accumulated contributions unless the member elects to withdraw the accumulated contributions in a lump sum.

Type of Final Average Salary - Average of highest five years.

Early Retirement (Age Reduction Factor Used)

Eligibility - Age fifty with fifteen or more years service.

Annual Amount - State pension is computed as regular retirement benefit but reduced one-tenth of 1% for each month age at retirement is between sixty and sixty-five and five-twelfths of 1% for each month under age sixty.

Deferred Retirement (Vested Benefit)

Eligibility - Ten years of service. Benefit commences at age sixty-five, or at age fifty if member has fifteen or more years of service.

Annual Amount - Computed as a regular retirement benefit with state pension based on service and final average salary at termination.

Regular Disability

Eligibility - Five years of service.

Annual Amount - \$125 per month plus \$5 for each year of service credit over five years.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002
(Continued)

Disability Retirement (No Reduction Factor For Age)

Eligibility - Five years of service and also qualify for Social Security Disability at time of termination.

Annual Amount - Computed as a regular retirement benefit with state pension based on service and final average salary at termination.

Duty Death Before Retirement

Eligibility - Fifteen years of service. Spouse to whom member had been married for two or more years is automatically eligible, or a dependent may be designated as beneficiary.

Annual Amount - Computed as regular retirement benefit but reduced in accordance with a 100% joint and survivor election.

Benefit Increases After Retirement: No automatic increases after retirement are provided. Unscheduled increases have been made from time to time.

Each member shall, as a condition of employment, contribute to the Fund 3% of his/her compensation. Effective July 1, 1986, each employing unit may elect to "pick up" the employee contribution. No part of the member contributions to the Fund picked up by the employer is includable in the gross income of the member. The "pick up" amount does count in the salaries used to determine the final average at retirement. Any member who leaves covered employment has the option to withdraw accumulated contributions and interest. In the event of a death of a member who has served less than fifteen years or does not meet the surviving spouse requirements, their designated beneficiary or estate is entitled to a lump sum settlement of their contributions plus interest.

Indiana pension statutes stipulates that each member of the Fund shall have the opportunity to direct their annuity savings account into one of five current investment programs:

1. The Guaranteed Fund - Interest is credited at a rate annually determined by the Board of Trustees. Principal and interest are "guaranteed." Market risk is assumed by the Fund.
2. The Bond Fund - Contains high quality fixed-income instruments which provide interest/capital gain income. Market risk is assumed by the member.
3. S&P 500 Index Fund - Closely tracks the return on the S&P 500 Index by employing an indexing strategy that invest in the stocks of the S&P 500 Index companies. Market risk is assumed by the member.
4. Small Cap Equity Fund - Consist of stocks with a market capitalization of less than \$1.5 billion. Market risk is assumed by the member.
5. International Equity Fund - Consists of securities of developed non-U.S. countries. Market risk is assumed by the member.

The Guaranteed Fund, Bond Fund, S&P 500 Index Fund, Small Cap Fund and International Fund are valued at market value. When a member retires, dies or suspends membership and withdraws from the fund, the amount credited to the member shall be valued at the market value of the member's investment plus accrued interest on investment less accrued investment expenses.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002
(Continued)

Members may only make a selection or re-allocation once per quarter. The changes will be in effect the first month of the quarter following the request for change. Members may request allocations to one or all of the approved funds, as long as those allocations are made in 10% increments of the total balance in the member's account at the time of allocation. The total must equal 100%.

Note 3. Employer Contributions Required and Employer Contributions Made

The Indiana State Teachers' Retirement Fund is funded on a "pay as you go" basis for employees hired prior to July 1, 1995. State appropriations are made for the amount of estimated pension benefit payout for each fiscal year. For employees hired on or after July 1, 1995, the individual employer will make annual contributions. These contributions are actuarially determined.

Based on the actuarial valuation at June 30, 2001, employer actuarially required contributions were \$572,226,197 normal cost, with no amortization of the unfunded actuarial accrued liability and zero provision for expenses. Contributions made by employers for the year ended June 30, 2002, totaled \$570,348,911 which was 17.2% of covered payroll.

Note 4. Cash, Investments and Securities Lending

Investments made by the Indiana State Teachers' Retirement Fund, including repurchase agreements, are summarized below. The investments that are represented by specific identifiable investment securities are classified as to credit risk by the three categories described below:

Category 1 includes investments that are insured or registered or for which securities are held by the State or its agent in the State's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or its agency in the State's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent but not in the State's name.

State statutes and Board of Trustees permit the Fund to lend securities to broker-dealers and other entities (borrowers) for collateral that will be returned for the same securities in the future. The Fund's custodial bank manages the securities lending program and receives securities or cash as collateral. The collateral securities cannot be pledged or sold by the Fund unless the borrower defaults, but cash collateral may be invested by the Fund. Collateral securities and cash are initially pledged at 102% of the market value of the securities lent. No more than 40% of TRF's total assets may be lent at any one time. At year-end, TRF has no credit risk exposure to borrowers because the amount TRF owes the borrowers exceed the amounts the borrowers owe TRF.

Approximately 25% of the securities loans can be terminated on demand either by the Fund or by the borrower, although generally the average term of these loans is one day. Cash collateral is generally invested in securities of a longer term, generally with maturities up to one year, and the weighted-average term to maturity of all collateral investments was thirty days.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS
June 30, 2002
(Continued)

	Category			Market Value
	1	2	3	
Equity Securities:				
Not on Securities Loan	\$ 2,142,293,187	\$ -	\$ -	\$ 2,142,293,187
On Securities Loan	-	82,253	-	82,253
Corporate Bonds:				
Not on Securities Loan	1,446,005,967	-	-	1,446,005,967
On Securities Loan	-	126,272,231	-	126,272,231
Foreign Bonds	12,718,800	-	-	12,718,800
U.S. Treasury and Agency Obligations:				
Not on Securities Loan	1,012,129,208	-	-	1,012,129,208
On Securities Loan	-	117,965,884	-	117,965,884
Investments on Securities Loan:				
Repurchase Agreements	427,180,111	-	-	427,180,111
Total Investments Categorized	<u>\$ 5,040,327,273</u>	<u>\$244,320,368</u>	<u>\$ -</u>	<u>\$ 5,284,647,641</u>

<u>Investments - Not Categorized</u>	<u>Market Value</u>
Investments Held by Broker-Dealers Under Securities Loans With Cash Collateral	
Equity Securities	\$ 108,656,376
U.S. Treasury and Agency Obligations	<u>425,686,218</u>
Total Investments Not Categorized	<u>\$ 534,342,594</u>

Note 5 Deferred Compensation Plan

The State offers its employees a deferred compensation plan (the plan) created in accordance with Internal Revenue Code Section 457. The plan, available to all State employees and employees of certain quasi-agencies and political subdivisions within the State, permits them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

All amounts of compensation deferred under the plan, all property and rights purchased with those amounts, and all income attributable to those amounts, property, or rights are (until paid or made available to the employee or other beneficiary) held for the exclusive benefit of participants of the plan and their beneficiaries as required by Section 457(g) of the Internal Revenue Code. In addition, the State has an Indiana Incentive Match Plan which provides \$15 per pay period for each employee who contributes to the 457 Plan.

The state has established a deferred compensation committee that holds the fiduciary responsibility for the plan. The committee holds the deferred amounts in an expendable trust.

INDIANA STATE TEACHERS' RETIREMENT FUND
NOTES TO FINANCIAL STATEMENTS

June 30, 2002

(Continued)

Note 6. Contingent Liabilities

The Indiana State Teachers' Retirement Fund is defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, the resolution of these matters will not have a material or adverse effect on the financial condition of the Fund. Tort claims are paid from the General Fund of the State of Indiana through the Attorney General's Office and are not paid by the Fund.

Note 7. Risk Management

The Fund is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; and natural disasters.

The policy of the Fund is not to purchase commercial insurance for the risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; job related illnesses or injuries to employees; and natural disasters.

Note 8. Employee Fund Membership

Employees of the Indiana State Teachers' Retirement Fund are now eligible for membership in the Fund. Effective July 1, 2001, IC 21-6.1-4-1(a)-10 states that members of the fund include persons who are employed by the fund.

INDIANA STATE TEACHERS' RETIREMENT FUND
REQUIRED SUPPLEMENTAL SCHEDULES
June 30, 2002

SCHEDULE OF FUNDING PROGRESS

(Dollar Amounts in Millions)

Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) Entry Age (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b-a)/c)
06-30-96	\$ 3,263	\$ 10,331	\$ 7,068	31.58%	\$ 2,879	245.50%
06-30-97	3,750	11,044	7,294	33.96%	2,985	244.36%
06-30-98	4,266	11,779	7,513	36.22%	3,095	242.75%
06-30-99	4,971	12,671	7,700	39.23%	3,294	233.76%
06-30-00	5,578	13,115	7,537	42.53%	3,193	236.05%
06-30-01	5,811	13,524	7,713	42.97%	3,319	232.39%

SCHEDULE OF CONTRIBUTIONS FROM THE EMPLOYERS
AND OTHER CONTRIBUTING ENTITIES

Valuation Date June 30	Annual Required Contribution	Percentage Contributed
1996	\$ 508,940,065	106%
1997	508,259,679	92%
1998	524,815,537	117%
1999	547,532,673	118%
2000	537,789,669	128%
2001	572,226,197	99%

**INDIANA STATE TEACHERS' RETIREMENT FUND
REQUIRED SUPPLEMENTAL SCHEDULES**

June 30, 2002
(Continued)

NOTES TO REQUIRED SUPPLEMENTAL SCHEDULES

The information presented in the required supplementary schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Valuation Date	June 30, 2001
Actuarial Cost Method	Entry Age Actuarial Cost Method
Amortization Method	Level Percent of Pay Closed
Amortization Period	38 Years
Asset Valuation Method	Market Value
Actuarial Assumptions:	
Investment Rate of Return	7.50%
Projected Salary Increases*	5.5%-10.6%
* Includes Wage Inflation at	5.50%
Cost of Living Adjustments	Unscheduled, Periodic Increases

**INDIANA STATE TEACHERS' RETIREMENT FUND
EXIT CONFERENCE**

The contents of this report were discussed on November 28, 2002, with Dr. William Christopher, Director. Our audit disclosed no material items that warrant comment at this time.